IN THE

Supreme Court of the United States

OCTOBER TERM, 1974

No. 74-542

UNITED STATES OF AMERICA, *Appellant*

v.

STATE TAX COMMISSION OF THE STATE OF MISSISSIPPI; ASBY BOBBY, Chairman; JIMMY WARREN, Tax Commissioner; WOODLEE OLIN, Ad Valorem Commissioner; KENNETH STEWART, Director of Alcoholic Beverage Control Division, Mississippi State Tax Commission; A. F. SUMNER, Attorney General, State of Mississippi; and the STATE OF MISSISSIPPI, *Appellees*

On Appeal from the United States District Court for the Southern District of Mississippi

BRIEF FOR THE APPELLEES

A. F. SUMNER
Attorney General
State of Mississippi

JAMES

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CITATIONS

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BRIEF FOR THE APPELLEES

ARGUMENT

Introduction

The appellant initially argued that Mississippi could not tax sales made on bases subject to exclusive federal jurisdiction because the 21st Amendment did not extend state jurisdiction. Relying upon *Collins* v. *Yosemite Park Co.*, 304 U.S. 518 (1938), this Court accepted that

argument but remanded the case for a ruling as to whether the 1940 Buck Act authorized such a tax.* The Court below has now found that the purpose of the Buck Act was to extend state taxing jurisdiction to such bases, for any tax measured by sales, and that Mississippi's wholesale mark-up is such a tax.

Appellant now argues that the Buck Act exempts military retailers from this tax because the tax is levied on them instead of upon sales to them; that collection of the tax from them by the suppliers who pay it, shifts the legal incidence to the retailers. The opinion below found the Buck Act's exemption (4 U.S.C. § 107(a)), inapplicable because the state's tax was levied upon wholesale sales and not upon the military purchasers. 378 F.Supp. 558, 568-69.

The Court below recognized, as we do, that the Buck Act's territorial extension of state sales tax jurisdiction left intact the constitutional freedom of federal instrumentalities from state action that interferes with federal functions. We shall support its decision by showing that the burden imposed on military retailing by Mississippi's wholesale mark-up is not an unconstitutional burden.

I. THE BUCK ACT AUTHORIZES THE TAX

A. The Tax Was Levied on Wholesale Sales

Mississippi has three levels of alcoholic beverage taxation. First, the state taxes consumers of beer, wine, and distilled spirits by levying a flat 5% tax on consumer purchases of all commodities. While the tax is normally collected and paid by retailers they must, by law, collect it from their purchasers, Miss. Code Ann. (1972) Sec. 27-65-17 and Sec. 27-65-31).

Second, the state taxes retailers of wine and spirits by imposing on them, gallonage taxes varying with alcoholic content from $.35 to $2.50 per gallon. Miss. Code Ann. (1972), Sec. 27-71-7. This tax is a fixed cost of doing business, included in the price paid by the retailers' customers. Its economic burden is passed on to the consumer, but its legal incidence is on the retailer. The retailer alone is bound by law to pay it and he pays it for the privilege of selling these beverages to consumers.

Third, the state taxes the business of wholesaling wine and spirits by levying a standard percentage mark-up on their wholesale cost. Miss. Code. Ann. (1972), Sec. 27-71-11. Any wholesale mark-up is necessarily included in the price charged to the retailer. While the economic burden of this tax is temporarily born by the retailer, who passes it on to the consumers, the tax must be paid by the wholesaler for the privilege of selling these beverages to retailers. Only the wholesaler, whether it be the state or a distiller, is liable for payment of this tax into the state treasury.

Mississippi's Alcoholic Beverage Commission has created by regulation, an option which allows the military retailers by buy either "direct from the distiller" (A. 37) or from the state, providing that when such direct purchases are made, the distiller shall first pay the wholesale mark-up to the state and then collect it from the purchaser. (A. 38).

The distiller's liability for the tax does not depend on its collection from the military retailers and is enforcible by revocation of the distiller's license to exploit Mississippi's market. No distiller is bound to sell to the military retailers but when it does it is

bound to pay the mark-up without any deduction for its wholesaling costs (Par. 13 Stipulation, A. 37). No distiller has protested or could protest this burden since it is voluntarily assumed.

Appellant's latest brief argues that the tax is discriminatory because the military retailers perform wholesaling services similar to those performed by Mississippi and the distillers. (p. 30) But the trial record discloses no such conduct nor is there any authorization for military wholesaling in the regulations here involved.

This argument seems to recognize that the tax is on wholesale transactions but the main thrust of appellant's argument is that what Mississippi meant to be a tax on wholesale sales is in law a tax on retailers. This Court's decisions do not permit such a distortion.

B. The Decisions of This Court Support the Constitutionality of the Tax

In our prior argument, we pointed out that *Collins* v. *Yosemite Park Co.*, 304 U.S. 518 (1938), had sustained a California wholesaler's excise tax on all liquor sales made to a federal concessionaire in Yosemite Park for resale there. That was a federal enclave where California had reserved taxing rights and this Court rejected our claim that the 21st Amendment permitted such taxation. The ground of decision was that the amendment had not extended the state's jurisdiction over federal enclaves. The California tax was upheld, this Court said, only because California had reserved its taxing rights in ceding the enclave. 412 U.S. 363, 375.

The Yosemite case was decided two years before the passage of the Buck Act. Instead of determining it-

self the Buck Act's effect on Mississippi's case, this Court remanded that question to the lower Court. 412 U.S. 363, 379. That Court has now considered the Buck Act and correctly found that the Buck Act makes taxing reservations as to federal enclaves unnecessary for any state tax *measured by sales.* This case is therefore now indistinguishable from the Yosemite case, insofar as a wholesalers' excise tax on sales made to a federal instrumentality for resale is concerned.

If, as the appellant now argues, the legal incidence of Mississippi's tax is upon a federal instrumentailty because it was collected from a federal retailer, the Yosemite case was wrongly decided. California's reservation of its power to tax such sales on a federal enclave and the Buck Act's general grant of state power to tax such sales, are both subject to the constitutional restriction against directly laying taxes on a federal instrumentality. The federal retailer in that case was just as much a federal instrumentality as the military retailers in this case. The fact that the tax was collected from a federal instrumentaility did not make it an unconstitutional tax, in either case. Both there and here the tax is saved from being an unconstitutional burden on the United States because it was levied on wholesale sales.

In the Yosemite case California's excise tax was collected directly from the federal retailer because it had bought its alcoholic beverages out of the state. That excise tax was imposed upon "all beer and wine sold in the state by a manufacturer or importer" and upon "all distilled spirits sold in the state by rectifiers or wholesalers," (304 U. S. 518, footnote 19 at 531-32). Payment had to be evidenced by revenue stamps, nor-

mally bought by an importer or wholesaler doing business in the state.

The California liquor control board had ruled that the federal retailer must buy the required stamps and thus pay the tax on these out of state purchases (Ibid. at p. 535-36). In upholding this ruling, the Court rejected a claim that collection of the tax not only interfered with an agent of the United States but was actually partly collected from the national government itself, because of its contractual interest in the profits of the federal retailer. The ground of rejection is equally applicable here, i.e., that the United States has consented to such a tax (Ibid at p. 536).

The Buck Act is just as effective federal consent to such sales taxation as the United States' acceptance of California's taxing reservation was in the Yosemite case.[1] Unless the Court is now prepared to overrule this aspect of the Yosemite decision, the decision below must be affirmed. Yet this Court's later decisions construing the Buck Act offer no basis for overruling its 1938 decision in the Yosemite case.

Whether sales of goods or services to the federal government are involved this Court has permitted state taxation of such transactions under the Buck Act. In 1954 the Court upheld the levy of a Louisville,

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[1] The Senate Report, No. 1625, 76th Cong., 3rd Session, reprinted in full as an appendix to this brief, states that the Buck Act was intended to nullify the 1937 holding in *James* v. *Dravo Contracting Co.*, 302 U.S. 134, that transactions on exclusive jurisdiction enclaves could not be taxed (*infra*, pp. 28-29). There is no mention of the 1938 holding in the Yosemite case referred to above. If, as appellant contends, the Buck Act was meant to exempt sales to federal retailers from such taxation, that more recent case would certainly have been noted as also nullified.

Kentucky, occupational tax, upon employees of a federal ordinance plant, located on an enclave over which the federal government had exclusive jurisdiction. *Howard* v. *Commissioners,* 344 U.S. 624. A dissent on the ground that the Buck Act did not grant consent to state taxation for the privilege of doing business with the United States was answered as follows: "The grant was given within the definition of the Buck Act and this was for *any tax* measured by net income, gross income, or gross receipts." 344 U.S. 624, 629.

Appellant's Point II (p. 31-33) wrongly assumes that the Buck Act did not wipe out all distinctions between exclusive and concurrent jurisdiction enclaves for state sales tax purposes. The Louisville case said it did. 344 U.S. 624, 627. That case held that assertion of a right to tax sales on federal enclaves does not interfere with any jurisdiction asserted by the federal government, whether its jurisdiction is exclusive or concurrent. If, on the other hand, a state tax is laid on a federal instrumentality, the Buck Act exemption applies alike to exclusive and concurrent jurisdiction enclaves.

Polar Ice Cream Co. v. *Andrews,* 375 U.S. 361 (1964), sustained a Florida wholesaler's tax on milk bought by post exchanges, measured by the volume sold. It construed that tax, as this one must be construed, as a tax levied on wholesaling. Although the economic burden was born by exchanges on exclusive jurisdiction enclaves, its collection from them by the wholesaler did not invalidate the tax. As to the Buck Act the Court said:

> "We think this provision provides ample basis for Florida to levy a tax measured by the amount of

milk Polar distributes monthly, including milk sold to the United States for use on federal enclaves in Florida." 375 U.S. 361, 383.

As the Navy's own post exchange regulations show, the Defense Department itself does not regard enforced collection of a tax on wholesale sales from an exchange purchaser as a tax on the exchange.[2] Appellant's argument impliedly assumes that some federal legislation must have given military retailers of liquor an immunity from state sales taxation that post exchanges do not have. We shall therefore consider what, if any, effect on the Buck Act resulted from passage of the Draft Extension Act in 1951, the federal statute authorizing military liquor sales.

C. Section 6 of the Draft Extension Act of 1951 Did Not Amend the Buck Act

The statutory authorization for selling liquor on military bases is Section 6 of the Draft Extension Act of 1951, 50 U.S.C. App. 473. That section authorizes the Secretary of Defense to establish criminally enforceable regulations applying to "sale consumption, possession of or traffic in" beer, wine or liquor "to or by" military personnel, "at or near" military bases.

Section 6 was a non-controversial amendment, adopted by agreement on April 13, 1951, just before the

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[2] Section 2634 of the Navy Exchange Manual states that a sales tax imposed on a supplier is valid, even where it is "his *obligation to collect* and pay it." (Emphasis ours) A.62. The Senate Report said as to non-appropriated fund instrumentalities, such as post exchanges, property "purchased from them" would be subject to state taxation if they were not to be federal instrumentalities. (See p. 30, *infra*.). But there is no suggestion that purchases by them would be exempt, in any event.

House passed the 1951 Draft Extension Bill, designated as S1, 82nd Congress (97 Cong. Rec. Part 3, p. 3914). This amendment was offered by Congressman Cole of New York as a substitute for an amendment offered a few minutes earlier by Congressman Bryson of North Carolina. Bryson's would have prohibited sale or possession of any beverage containing an alcoholic content of more than one-half of one percent at any selective service training camp. Ibid, p. 3902. Cole then offered his substitute amendment as better adapted to dealing with military alcoholic beverage problems, because Bryson's "applies only to the Training Corps and not to all camps and posts of the armed forces." Ibid. p. 3902. This history conclusively established this section as a temperance measure; not meant to provide the armed forces with tax-free liquor. Certainly if this statute had been meant to divest the states of their control of purchase or importation it would have said so and could not have been enacted without debate.

The Secretary's regulation (A. 31-36) directs the military purchasers to consider all factors, including price (A. 33, 35). But an initial direction in the regulation to seek supplies "without regard to state law," was withdrawn before Mississippi adopted its regulation (A. 35). Neither the regulation nor the authorizing statute mentions taxation.

Section 6 of the Draft Extension Act was no more an amendment of the Buck Act than the Soldiers and Sailors Civil Relief Act was. In *Sullivan* v. *United States,* 395 U.S. 169 (1969), a serviceman claimed that this 1942 Act had relieved him of state sales and use taxes on merchandise purchased from private sellers. The Court held that it did not, basing its ruling on the

fact that the Relief Act says nothing about sales or use taxes, which had been explicitly dealt with in 1940 in the Buck Act.[3] The Court construed the Buck Act's federal instrumentality exemption as follows:

> "In the 1940 Buck Act, Congress provided that the States have 'full jurisdiction and power to levy and collect' sales and use taxes in 'any federal area,' except with respect to the sale or use of property *sold by* the United States or its instrumentalities through commissaries, ship's stores, and the like." 395 U.S. 169, 178 (Emphasis ours).

Like the 1942 Relief Act, the 1951 Draft Extension Act, said nothing about any of the matters dealt with in the Buck Act and was certainly not meant to give military retailers of liquor a freedom from taxation of their *purchases* not enjoyed by military retailers of necessities such as milk.

In short, the Buck Act authorized state taxation of sales of alcoholic beverages to federal agencies on enclaves where United States jurisdiction is territorially exclusive. We now turn to the doctrine of sovereign immunity, as it applies to taxation of dealers in alcoholic beverages.

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[3] The exemption provided was from state taxation of a serviceman's personal property outside his home state and this Court noted the traditional distinction between property taxes and taxes "on the privilege of selling or buying property." 395 U.S. 169, 175. That distinction is ignored by appellant in its reliance on *United States* v. *County of Allegheny*, 322 U.S. 174 (1943). (p. 15) The reasons for the distinction are discussed in *Esso Standard Oil Co.* v. *Evans*, 345 U.S. 495, 499-500 (1952). That case distinguished the Allegheny County case in upholding a tax on the privilege of storing gasoline owned by the United States.

II. THE TENTH AND TWENTY-FIRST AMENDMENTS SUSTAIN THE TAX

The 21st Amendment was passed to end the failed experiment in federal liquor control that the 18th had made possible. Whatever else it may have done, the 21st restored to the states all of the powers over the liquor traffic that they had before the 18th. One traditional method of exercising such power has been exclusive state operation and ownership of the business of wholesaling alcoholic beverages. Another such method has been excise taxation of state licensed private wholesalers.

As we have shown, in the Yosemite case this Court allowed California to collect its excise tax on all sales to a federal concessionaire, while denying California the right to collect license fees from that federal instrumentality. The Buck Act was passed two years after that decision and California now collects its excise tax on sales made to all federal enclaves within the state. See California Revenue and Taxation Code. Sec. 32201. It also collects the tax upon purchases made from out-of-state suppliers by federal hospitals located in the state. See *National Distillers* v. *State Board,* 83 Cal. App. 2nd 35, 187 Pac. 2d 821 (1947).

Appellant's brief mistakenly assumes that the 10th Amendment has no application to this case. This Court has said that state liquor laws derive their force "from power originally belonging to the states and preserved to them by the 10th Amendment."[4] *McCormick & Co.* v. *Brown,* 286 U.S. 131, 141 (1932).

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[4] That amendment "reserved to the States" the "powers not delegated to the United States by the Constitution, nor prohibited by it to the States."

In that case the Court held that even during national prohibition, when federal law played the main role in controlling the liquor traffic, West Virginia could define intoxicating liquor in a more stringent way than the United States had, in deciding what products could be brought into the state. After repeal, the Court again affirmed state supremacy in the field of liquor control under the 10th Amendment. *United States* v. *Constantine,* 296 U.S. 287, 295-96 (1935). There the Court held that the federal government's power to tax retail liquor dealers did not permit the United States to impose a *punitive tax,* based on a dealer's violation of state law.

A state's Tenth Amendment right to tax liquor sales is not limited by the Supremacy Clause. The Constitution allows the United States to tax liquor for its purposes but does not preclude taxation by a state for its purposes. Each state has so far maintained its own tax policy with respect to liquor sales without interference from the federal government. While the recent case of *Heublein, Inc.* v. *South Carolina Tax Commission,* 409 U.S. 275 (1972) was not decided upon constitutional grounds, it is an example of the kind of deference to state liquor taxation that both the 10th and 21st Amendments were meant to assure.

South Carolina taxes both wholesale sales of liquor and the net income derived by national distillers upon their sales to the state's wholesalers. Heublein contended that this income tax violated a federal statute designed to limit state taxation of a national business's net income because South Carolina compelled Heublein to engage in taxable business activity within the state that served no business purpose of Heublein. South

Carolina required that the initial sale by Heublein be made to a local agent, who then ships to its wholesalers from a state licensed warehouse. Ibid at 278. This requirement was sustained as "reasonably related" to the state's liquor control purposes. Ibid at 283.

But federal deference to state liquor control stops short of an immunity from federal taxation of state wholesaling monopolies, such as Mississippi's. *Ohio* v. *Helvering,* 292 U.S. 360 (1934), established that when a sovereign state engages in a business to raise revenue, non-discriminatory federal taxation of the business is not an unconstitutional burden on sovereignty. In that case, Ohio sought to avoid the imposition of license fees and the federal excise tax on liquor bought by the state for resale through state-owned stores. Since these stores were instrumentalities by which Ohio exercised "governmental powers" (Ibid at 368) Ohio claimed that federal taxation of its liquor business impaired its sovereignty. The Court answered that when a state chooses to engage in business, that "is not the performance of a governmental function" (Ibid at 369) and the tax was sustained.

Intergovernmental tax immunity doctrine is "a principle resulting from our dual system of government." *Ohio* v. *Helvering,* 292 U.S. 360, 368. The reasoning and practical criteria adopted by the Court in determining exemption from a federal tax "are clearly applicable to a state tax on earnings under a contract with the Federal Government." *James* v. *Dravo Contracting Co.,* 302 U.S. 134, 157 (1937). Appellant's argument implies that there is some reason of constitutional policy for holding that Mississippi's taxation of sales to federal retailers illegally burdens a sovereign function, while federal

taxation of state-owned retailers does not. We shall therefore note below the similarities and differences in the impact on sovereign functions of Mississipp's tax and the federal excise tax.

First, Mississippi buys and sells liquor at a profit with the net proceeds of the operation going into Mississippi's treasury and becoming usable for all state purposes. Miss. Code Ann. (1972) Sec. 27-71-29. The military retailers in Mississippi operate with non-appropriated funds and the profits of their operations never reach the federal treasury (A. 30).

Second, Mississippi's profits are used to supply essential public services used by all persons residing within the state, whether military or civilian, temporary or permanent. The military retailers' profits are used for the exclusive benefit of the particular mess or club that generates them (A. 40-41). These benefits are no more essential to the maintenance of armed services' morale than the public services provided by Mississippi's taxes are.

Third, Mississippi's wholesale mark-up is applied uniformly to all retail liquor businesses in the state, military and civilian. But Mississippi exempts the military from its consumers' sales tax and its retailers excise tax (A. 36) allowing the military retailers to both sell and buy liquor at substantially lower prices than private retailers. The federal excise tax is also uniformly applied to all distilled spirits, whether bought by state or private wholesalers, but there is no forgiveness of any federal taxes on the state's business. Thus while Misissippi discriminates in favor of the military retailers the United States does not discriminate in Mississippi's favor.

Fourth, Mississippi's mark-up is an element of cost that is passed on to retail purchasers and their customers. The federal excise tax is also an element of cost that is presently passed on to both military and civilian customers of all retailers. But if the United States wished to assure its military personnel of even lower liquor prices than they now get from the military retailers it could, of course, rebate to military purchasers all or a part of its $10.50 per proof gallon tax on distilled spirits. See 26 U.S.C. Sec. 5001(a)(1).

One way to see the policy questions raised by the appellant's argument is to try and visualize the Congressional debate that such a proposal might provoke. The Congress would first be asked to decide whether liquor should be retailed on military bases at prices more than ten percent below those charged by civilian retailers in the same area; the limitation now stated in 3(b) of the Defense Department regulations (A. 34). Debate would then occur as to whether this should be done at the expense of state or federal liquor revenues or both. A policy judgment would only emerge after due consideration of the impact of such reduced liquor prices upon the welfare of military personnel and upon the welfare of the states. Whether any resulting federal invasion of a state's right to control the liquor traffic within its borders violated the 10th or 21st Amendments would then be left for determination by this Court.

This Court has recognized that the complex problems raised by such political and economic considerations "are ones which Congress is best qualified to resolve." *United States* v. *Detroit*, 355 U.S. 466, 474 (1958). Yet the appellant is asking this Court to originate a policy in favor of extraordinarily low prices for federal

military personnel at the expense of state revenues alone. Dressing the argument in the language of constitutional debate cannot disguise the true nature of the issue; which is, may this Court declare as federal policy a matter properly resolvable by the Congress?

Moreover, the invitation for a judicial resolution of this controversy is remarkably belated. Another monopoly state, Michigan, amended its Liquor Control Act on May 5, 1954, to require the military to purchase from the state stores and authorized its Liquor Control Commission to give the military retailers a discount from the state stores' retail prices.[5] On May 17, 1954, the Michigan Commission issued the following order:

> "DISTILLED SPIRITS VENDORS AND THEIR REPRESENTATIVES
>
> Attention: Executive office in charge of Monopoly State Operations
>
> An Amendment to Section 16 of the Michigan Liquor Law, effective May 5, 1954, provides that military installations must now purchase all spirits from the State Stores of the Michigan Liquor Control Commission and cannot purchase directly from the distillers as has been the practice in the past.
>
> Therefore, the Liquor Control Commission has ordered that effective June 1, 1954, no further

[5] Section 3 of Michigan Liquor Control Act of August 8, 1933, prohibited importation of liquor into the state "unless the sale or delivery is made by the Commission or its authorized agent or distributor." Michigan Statutes Annotated, 18.973. Public Acts 1954, No. 175, applied this policy to "military establishments located in the state" by authorizing the Commission to establish prices on sales to them" by rule or regulation." Michigan Statutes Annotated 18.987.

shipments shall be made by any distillers directly to the aforementioned installations. Any sales made beyond June 1, 1954, will constitute a violation of the Michigan law and subject the distiller to stringent penalties."

Michigan has thus been collecting a wholesale mark-up [6] from all the military bases in that state, about five times the number in Mississippi, for more than 20 years without any legal challenge from the Defense Department. [7]

No explanation has been offered as to why the Department delayed its attack on a monopoly state's right to apply its mark-up to military sales for fifteen years. It is also odd that the aim of this appeal, even lower liquor prices for military retailers than they are now paying, contradicts the aims of the Department stated in this record. In his initial memorandum summing up the Department's position as to price negotiations with the monopoly states, Assistant Secretary Morris said that a satisfactory price was one which would allow "an adequate profit to the installation." (Ex. 8, A. 44) [8] No attempt was made below

[6] Like Mississippi, Michigan fixes the amount of the state's mark-up on sales to military bases by regulation. However, Michigan fixes the amount by allowing a 22% discount from the prices charged by its stores to their retail customers. See Rule 436.601.

[7] The memorandum from Navy Under Secretary Baldwin to Defense Assistant Secretary Morris, dated April 22, 1966 (Exhibit 9, A. 46) states that the "net mark-ups over costs to state stores imposed upon Military Messes" then imposed by Michigan, Oregon, and Washington were about 30%, 70%, and 45% respectively. Yet there has been no legal challenge to any of these other monopoly state mark-ups.

[8] In his final memorandum (Exhibit 13) he said the deletion of the language "without regard to prices locally established by state statute or otherwise," "would not require nor would it preclude

to show that Mississippi's regulation, which gave the military retailers both profits and a lower price than private retailers pay, did not yield an "adequate profit." The case was prosecuted on the theory that the price could not lawfully include any state mark-up, no matter how reasonable it might be.

Since military functions are involved we shall examine in the next section, this Court's intergovernmental tax immunity doctrine, as applied to military expenditures.

III. THE TAX IMMUNITY DECISIONS OF THIS COURT DO NOT BAR STATE SALES TAXATION THAT INCREASES DEFENSE COSTS

A turning point in the development of intergovernmental tax immunity doctrine was *James* v. *Dravo Contracting Co.*, 302 U.S. 134 (1937). In that case West Virginia taxed a construction contractor's receipts from work performed for the federal government on federal enclaves.

After noting that close distinctions must be made in tax immunity cases "without unduly limiting the taxing power which is equally essential to both nation and state under our dual system (Ibid at 150), the opinion comprehensively reviews the Court's prior decisions in this field (Ibid at 151-161). It then concluded, as to concurrent jurisdiction enclaves, that notwithstanding the resulting increased cost of federal projects, the tax did not "interfere in any substantial way with the performance of federal functions and is

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negotiations with the states for the most advantageous contract with the Government." (A. 56). Yet the complaint alleged that mere collection of the mark-up was unlawful, with no allegation that the military retailers had tried to negotiate more advantageous mark-up (A. 6-11).

a valid exaction." Ibid at 161. As to the enclaves whether the federal government had exclusive jurisdiction the Court held that these contractor's receipts were beyond the state's taxing power. Ibid at 140. It was this latter aspect of the decision that Congress nullified by the Buck Act. (*Infra,* pp. 28-29).

Ever since *James* there has been no doubt that a non-discriminatory state tax on sales to the United States, does not unconstitutionally burden a federal function. This issue arose again in *Alabama* v. *King and Boozer,* 314 U.S. 1 (1941), when the Solicitor General tried to limit *James* to its own facts. The Solicitor General agreed with the *James* "legal incidence" test for valid state taxation of federal contractors, as opposed to "economic incidence." However, the Solicitor General argued that the legal incidence of Alabama's sales tax was on the federal government because the federal government was legally bound to pay it.

The Court adhered to its legal incidence test but rejected the result the Solicitor General urged upon it. While the Court recognized that a cost-plus contract legally bound the federal government to pay the amount of the tax to the contractor, this fact merely determined the economic incidence of the tax and was therefore irrelevant. Since the intention of the state was to tax the contractor's business, the fact that he in turn was doing business with the United States on a cost-plus basis could not shift the legal incidence to the federal government.

That case was a sound application of *James,* and as the Court below noted, it has never been overruled. 378 F.Supp. 558, 566. As in *James* and *King & Boozer* the tax here was added to the cost of federal

procurement but was not aimed at any function performed by the United States. It stemmed instead from Mississippi's lawful control of a wholesale liquor business. Unlike the increase in military construction costs resulting from the state tax sustained in *King & Boozer,* Mississippi's tax has been applied only to military *purchases for resale* with the economic burden passed on to the ultimate consumer.

Appellant's reliance on *First Agricultural National Bank* v. *State Tax Commission,* 392 U.S. 339 (1968), as a constitutional law holding is unwarranted. The Court never even reached "the constitutional question of whether today national banks should be non-taxable as federal instrumentalities." Ibid at 341. The Court held that national banks had a congressionally established immunity from all forms of state taxation except as to real property and bank shares (Ibid at 346) and declined to apply to the Bank's purchases a Massachusetts retail sales tax levied, like Mississippi's retail sales tax, on purchasers. Ibid at 348. As the Court below pointed out, Mississippi's wholesale mark-up was a tax levied on wholesale sales, instead of on purchasers, and the bank case is also inapposite for that reason. 378 F.Supp. 558-69.

Mississippi's law and regulation merely established a percentage wholesale mark-up without fixing wholesale prices. Enforcement could not prevent practical absorption by a distiller's reduction of its wholesaler's price. Mississippi could only insist that the distiller try to collect whatever sum was designated on the invoice as the mark-up and that the mark-up be the stipulated percentage of what the invoice showed as the wholesaler's price.

We do not disagree with appellants contention that the practical effect was to require the private suppliers to sell the military retailers "at a total price, including the mark-up, that *approximates* the state's price for the same product." (Emphasis ours, p. 36). But if there was any other reason for dealing directly with the distillers than an opportunity to shave the state's price it does not appear in this record. [9]

Thus Mississippi's mark-up bears no resemblance in its legal or practical effect to Massachusetts' sales tax. Nor can any rational contention be made that the Buck Act's exemption was meant to have a practical or legal effect comparable to the statutory exemption of national banks. [10]

We respectfully submit that no theory of intergovernmental tax immunity ever sanctioned by this Court could relieve these military retailers from payment of Mississippi's non-discriminatory wholesale mark-up, on their purchases of alcoholic beverages.

IV. THERE IS NO CONFLICT BETWEEN MISSISSIPPI'S REGULATION AND FEDERAL PROCUREMENT POLICY

Appellant argues that the tax impermissably interfers with federal procurement policy because it restricts price competition for the business of federal retailers. This argument is not based upon the federal statutory policy in favor of competitive procurement,

[9] The military retailers offered no evidence as to why they deemed dealing directly with distillers more advantageous than dealing with the State.

[10] Appellant's reliance on *Kern-Limerick, Inc.* v. *Scurlock*, 347 U.S. 110, is even less rational. The Arkansas statute in that case expressly exempted purchases by the United States (*Ibid.* at 112) and the Court construed the Armed Services Procurement Act as making the United States the purchaser in question. *Ibid.* at 116.

which does not apply to non-appropriated fund instrumentalities. *Paul* v. *United States,* 371 U.S. 245, 269. The sole basis for the argument is the Secretary of Defense's regulation directing military purchasers to obtain "the most advantageous contract, price, *and other factors considered.*" (A. 33). (Emphasis ours.)

There is no conflict between this directive and Mississippi's tax policy because the directive does not mention taxes. Moreover, Mississippi permits unlimited competition between distillers in pricing their products. The only restriction is that the prices to all retailers shall be a standard and reasonable percentage of a wholesaler's price, individually set by the distillers. 378 F.Supp. 558, 572.

The regulation's option to purchase from the state at the standard percentage over wholesaler's cost, established a price ceiling for the military retailer's direct purchases from distillers that could hardly be called disadvantageous. The factor of compliance with state law by payment of a non-discriminatory wholesale sale tax, is an inescapable factor for consideration.

Another factor is the aspect of unfair competition considered in the Defense Department's own regulation. In restricting resale prices to not more than ten percent below those of civilian retailers in the same area (A. 34), the Department recognized the desirability of preventing cut-throat competition with private enterprise. In view of the substantially lower prices at which military purchases were made, as a result of their exemption from the state's gallonage taxes, it is apparent that even lower prices might have encouraged lower resale prices than the regulation permits. The Defense

Department's stated aim of reasonable profits would be changed to exorbitant profits if an even greater profit margin were added to the economies provided by operating on government property.

Competition between wholesalers is of course prevented by Mississippi's pre-emption for itself of the state's wholesale liquor business. But the legality of such pre-emption was established in 1898 in *Vance* v. *Vandercook,* 170 U.S. 438 and again recognized in 1934 in *Ohio* v. *Helvering,* 292 U.S. 360.

The cases cited by appellant that invalidated state regulations are all based upon an explicit conflict with federal statutes and do not concern alcoholic beverages. It there were such a conflict here, we believe that the 10th and 21st Amendments would resolve it in favor of the state. But in the absence of such a conflict there is no state-federal policy argument for this Court to resolve.

CONCLUSION

We respectfully submit that the three-judge court's decision was squarely based upon this Court's decisions and should be affirmed.

Respectfully submitted,

A. F. SUMMER
Attorney General
State of Mississippi

JAMES H. HADDOCK
Chief Attorney, Mississippi Tax Commission

ROBERT L. WRIGHT
Washington, D. C.
Special Counsel to the Mississippi State Tax Commission

APPENDIX

APPENDIX

76TH CONGRESS, 3D SESSION

SENATE

REPORT NO. 1625

APPLICATION OF STATE SALES, USE, AND INCOME TAXES TO TRANSACTIONS IN FEDERAL AREAS

MAY 16 (legislative day, APRIL 24), 1940—
Ordered to be printed

MR. GEORGE, from the Committee on Finance, submitted the following

REPORT

[To accompany H.R. 6687]

The Committee on Finance, to whom was referred the Bill (H.R. 6687) to authorize the levy of State, Territory, and District of Columbia taxes upon, with respect to, or measured by sales, purchases, or use of tangible personal property or upon sellers, purchasers, or users of such property measured by sales, purchases, or use thereof occurring in United States national parks, military and other reservations or sites over which the United States Government may have jurisdiction, having considered the same, report favorably thereon with amendments and recommend that the bill as amended do pass.

GENERAL STATEMENT

This bill passed the House at the first session of the Seventy-sixth Congress and was referred to the Committee on Finance which reported it to the Senate with certain clarifying changes on July 28, 1939. Due to certain objec-

tions being raised to the bill by various departments in the executive branch of the Government after the bill had been reported to the Senate, it was recommitted to the Committee on Finance for further study and recommendation. Your committee, through a subcommittee composed of Senators George, Brown, and La Follette, held a hearing on April 23, 1940, at which time representatives of the various State taxing authorities appeared in favor of the bill and representatives of the War and Navy Departments and of the Department of the Interior appeared in opposition to certain features of the bill.

Upon completion of the hearings, the subcommittee suggested that a conference be held by the representatives of the State agencies and the Federal agencies with a view to recommending to said subcommittee any proposal or proposals upon which said representatives could agree. Such a conference was held and the proposals which were submitted were used as a point of departure by the subcommittee in drafting the amendment reported by your committee.

In general, the bill, as amended, proposes to do three things. First, it provides that State sales and use taxes (with certain exceptions which are hereafter explained) shall be applicable with respect to transactions occurring within Federal areas in the same manner and to the same extent as they are applicable with respect to transactions occurring outside such areas and within the State. Second, it provides that State income taxes shall be applicable with respect to persons residing within a Federal area or receiving income from transactions occurring or services performed in such area in the same manner and to the same extent as they are applicable with respect to persons residing outside such area or receiving income from transactions occurring or services performed outside such area. Third, it contains certain clarifying amendments to section 10 of the Federal Highway Act of June 16, 1936

(known as the Hayden-Cartwright Act permitting State taxation of sales of gasoline and other motor-vehicle fuels sold in Federal areas for private purposes), and provides that the tax levied and collected under that section shall continue to be levied and collected under that section, as amended, rather than under the authority contained in section 1 of this bill.

Detailed Explanation of the Bill

Section 1(a) of the committee amendment removes the exemption from sales or use taxes levied by a State, or any duly constituted taxing authority in a State, where the exemption is based solely on the ground that the sale or use, with respect to which such tax is levied, occurred in whole or in part within a Federal area. At the present time exemption from such taxes is claimed on the ground that the Federal Government has exclusive jurisdiction over such areas. Such an exemption may be claimed in the following types of cases: First, where the seller's place of business is within the Federal area and a transaction occurs there, and, second, where the seller's place of business is outside the Federal area but delivery is made in Federal area and payment received there. This section will remove the right to claim an exemption because of the exclusive Federal jurisdiction over the area in both of these situations. The section will not affect any right to claim any exemption from such taxes on any ground other than that the Federal Government has exclusive jurisdiction over the area where the transaction occurred.

This section also contains a provision granting the State or taxing authority full jurisdiction and power to levy and collect any such sale or use tax in any Federal area within such State to the same extent and with the same effect as though such area was not a Federal area. This additional authorization was deemed to be necessary so as to make it clear that the State or taxing authority had power to levy

or collect any such tax in any Federal area within the State by the ordinary methods employed outside such areas, such as by judgment and execution thereof against any property of the judgment-debtor.

Subsection (b) of section 1 provides that the taxes to be levied and collected under this section shall be applicable only with respect to sales or purchases made, receipts from sales received, or storage or use occurring, after June 30, 1940.[6]

Section 2(a) of the committee amendment removes the exemption from income taxes levied by a State, or any duly constituted taxing authority in a State, where the exemption is based solely on the ground that the taxpayer resides within a Federal area or receives his income from transactions occurring or services performed in such area. One of the reasons for removing the above exemption is because of an inequity which has arisen under the Public Salary Tax Act of 1939. Under that act a State is permitted to tax the compensation of officers and employees of the United States when such officers and employees reside or are domiciled in that State but is not permitted to tax the compensation of such officers and employees who reside within Federal areas within such State. For example, a naval officer who is ordered to the Naval Academy for duty and is fortunate enough to have quarters assigned to him within the Naval Academy grounds is exempt from the Maryland income tax because the Naval Academy grounds are a Federal area over which the United States has exclusive jurisdiction; but his less fortunate colleague, who is also ordered there for duty and rents a house outside the academy grounds because no quarters are available inside, must pay the Maryland income tax on his Federal salary. Another reason for removing the above exemption,

[6] The Bill was not passed until October 9, 1940 and the effective date was changed accordingly to December 31, 1940, 54 Stat. 1060.

is that under the doctrine laid down in *James V. Dravo Contracting Co.* (302 U.S. 134, 1937), a State may tax the income or receipts from transactions occurring or services performed in an area within the State over which the United States and the State exercise concurrent jurisdiction but may not tax such income or receipts if the transactions occurred or the services were performed in an area within the State over which the United States has exclusive jurisdiction.

This section contains, for the same reasons, a similar provision to the one contained in section 1 granting the State or taxing authority full jurisdiction and power to levy and collect any such income tax in any Federal area within such State to the same extent and with the same effect as though such area was not a Federal area.

Subsection (b) of section 2 provides that the taxes to be levied and collected under this section shall be applicable only with respect to income or receipts received after June 30, 1940. Your committee, upon recommendation of the representatives of the State taxing authorities, has made the effective dates of both section 1 and section 2 the same for ease in administration and to prevent the income tax section from becoming effective retroactively. The definition of income tax is broad enough to include a sales tax which is measured by gross receipts from sales. To fix an earlier effective date for the income tax section than for the sales tax section would thus result in having different effective dates for the same tax, in some cases, and would also permit the retroactive application of such sales taxes.

Section 3 of the committee amendment provides that sections 1 and 2 shall not be deemed to authorize the levy or collection of any tax on or from the United States or any instrumentality thereof. This section also provides that sections 1 and 2 shall not be deemed to authorize the levy or collection of any tax with respect to sale, purchase,

storage, or use of tangible personal property sold by the United States or any instrumentality thereof to any authorized purchaser. An authorized purchaser being a person who is permitted, under regulations of the Secretary of War or Navy, to make purchases from commissaries, ship's stores, or voluntary unincorporated organizations of Army or Navy personnel, such as post exchanges, but such person is deemed to be an authorized purchaser only with respect to such purchases and is not deemed to be an authorized purchaser within the meaning of this section when he makes purchases from organizations other than those heretofore mentioned.

For example, tangible personal property purchased from a commissary or ship's store by an Army or naval officer or other person so permitted to make purchases from such commissary or ship's store, is exempt from the State sales or use tax since the commissary or ship's store is an intrumentality of the United States and the purchaser is an authorized purchaser. If voluntary unincorporated organizations of Army and Navy personnel, such as post exchanges, are held by the courts to be instrumentalities of the United States, the same rule will apply to similar purchases from such organizations; but if they are held not to be such instrumentalities, property so purchased from them will be subject to the State sales or use tax in the same manner and to the same extent as if such purchase was made outside a Federal area. It may also be noted at this point that if a post exchange is not such an instrumentality, it will also be subject to the State income taxes by virtue of section 2 of the committee amendment.

Section 4 of the committee amendment was inserted to make certain that the criminal jurisdiction of Federal courts with respect to Federal areas over which the United States exercised exclusive jurisdiction would not be affected by permitting the States to levy and collect sales, use, and income taxes within such areas. The provisions of this sec-

tion are applicable to all Federal areas over which the United States exercise jurisdiction, including such areas as may be acquired after the date of enactment of this act.

Section 5 of the committee amendment provides that section 1 and 2 shall not be deemed to authorize the levy or collection of any tax on or from any Indian not otherwise taxed.

Section 6 contains the definitions of the terms used in the committee amendment.

Subsection (a) defines the term "person" as it is defined in section 3797 of the Internal Revenue Code to mean and include an individual, trust, estate, partnership, company, or corporation.

Subsection (b) defines the term "sales or use tax" but excepts from such definition a tax with respect to which the provisions of section 10 of the Federal Highway Act of June 16, 1936, are applicable. Section 10 of that act, commonly known as the Hayden-Cartwright Act, permits State taxation of sales of gasoline and other motor-vehicle fuels sold in Federal areas for private purposes. Your committee thought it desirable that the provisions of that act should be continued in effect without regard to the provisions of section 1 of the committee amendment and therefore any State tax which is imposed on sales of gasoline and other motor-vehicle fuels will continue to be imposed on such sales in Federal areas under the provisions of section 10 of that act, as amended by section 7 of the committee amendment, rather than under the provisions of section 1 of the committee amendment.

Subsection (c) defines the term "income tax" to mean any tax levied on, with respect to, or measured by, net income, gross income, or gross receipts. This definition, as well as the preceding definition of sales or use tax must of necessity cover a broad field because of the great varia-

tions to be found between [illegible] intent of your committee in [illegible] definition was to include therein any State tax (whether known as a corporate-franchise tax, or business-privilege tax, or by any other name) if it is levied on, with respect to, or measured by, net income, gross income, or gross receipts.

Subsection (d) defines the term "State" to include any Territory or possession of the United States. The District of Columbia was not included in the definition since Congress is the local legislature for the District and any Sales, use or income taxes enacted for the District are applicable in all areas within said District.

Subsection (e) defines the term "Federal area" to mean any lands or premises held or acquired by or for the use of the United States or any department, establishment, or agency of the United States. Any Federal area, or any part thereof, which is located within the exterior boundaries of any State is deemed to be a Federal area within such State for the purposes of this act. For example, Yellowstone National Park is a Federal area which is located wtihin the exterior boundaries of three States (Wyoming, Montana, and Idaho) and therefore, for the purposes of this act, that part of the Park which falls within the exterior boundaries of Wyoming will be included within Wyoming's taxing jurisdiction, that part which falls within Montana will be included within Montana's taxing jurisdiction, and that part which falls within Idaho will be included within Idaho's taxing jurisdiction.

Section 7(a) of the committee amendment amends section 10 of the Hayden-Cartwright Act so that the authority granted to the States by such section 10 will more nearly conform to the authority granted to them under section 1 of this act. At the present time a State such as Illinois, which has a so-called gallonage tax on gasoline based upon the

privilege of using the highways in that State, is prevented from levying such tax under the Hayden-Cartwright Act because it is not a tax upon the "sale" of gasoline. The amendments recommended by your committee will correct this obvious inequity and will permit the levying of any such tax which is levied "upon with respect to, or measured by, sales, purchases, storage, or use of gasoline or other motor vehicle fuels."

Subsection (b) of section 7 is a clarifying amendment to such section 10 restating what was the obvious intent of the original act.

Your committee has also amended the title of the bill to conform to the changes made in the text.